

VZCZCXRO7170
PP RUEHAG RUEHROV RUEHSL RUEHSR
DE RUEHUP #0843/01 3281448
ZNY CCCCC ZZH
P 241448Z NOV 09
FM AMEMBASSY BUDAPEST
TO RUEHC/SECSTATE WASHDC PRIORITY 4680
INFO RUCNMEM/EU MEMBER STATES COLLECTIVE PRIORITY
RUEHAK/AMEMBASSY ANKARA PRIORITY 0240
RUEHAH/AMEMBASSY ASHGABAT PRIORITY 0087
RUEHGB/AMEMBASSY BAGHDAD PRIORITY 0104
RUEHKB/AMEMBASSY BAKU PRIORITY 0171
RUEHBW/AMEMBASSY BELGRADE PRIORITY 0020
RUEHKV/AMEMBASSY KYIV PRIORITY 0175
RUEHMO/AMEMBASSY MOSCOW PRIORITY 0737
RUEHVJ/AMEMBASSY SARAJEVO PRIORITY 0301
RUEHSQ/AMEMBASSY SKOPJE PRIORITY 0693
RUEHTI/AMEMBASSY TIRANA PRIORITY 0484
RUEHVB/AMEMBASSY ZAGREB PRIORITY 1211
RUEAIIA/CIA WASHINGTON DC PRIORITY
RUCPDO/DEPT OF COMMERCE WASHDC PRIORITY
RHMCSUU/DEPT OF ENERGY WASHINGTON DC PRIORITY
RHEFDIA/DIA WASHINGTON DC PRIORITY
RUEHBS/USEU BRUSSELS PRIORITY
RHEHNSC/WHITE HOUSE NSC WASHDC PRIORITY

C O N F I D E N T I A L SECTION 01 OF 06 BUDAPEST 000843

SIPDIS

STATE FOR AMB MORNINGSTAR, EUR/CE JMOORE, EUR/FO, EUR/ERA,
EUR/RUS, EEB/FO, PLEASE PASS TO NSC JHOVENIER

E.O. 12958: DECL: 11/24/2019

TAGS: [ENRG](#) [ECON](#) [EPET](#) [PGOV](#) [PREL](#) [OREP](#) [HU](#)

SUBJECT: AMBASSADOR MORNINGSTAR'S CONSULTATIONS IN BUDAPEST

REF: A. BUDAPEST 265

[1](#)B. BUDAPEST 320

[1](#)C. ZAGREB 670

Classified By: EconOff Jeffrey M. Jordan, reasons 1.4 (b),(d)

[1](#)1. (SBU) Summary: Special Envoy for Eurasian Energy Ambassador Richard Morningstar visited Budapest on November 16-17 to take part in the "Fourth Energy Forum," a conference dedicated to fostering a broad discussion on European energy security. While in Budapest, Ambassador Morningstar met with a range of government and business leaders, including Prime Minister Bajnai, former Prime Ministers Orban and Topolanek, and MOL CEO Hernadi. Ambassador Morningstar consistently conveyed the message that Europe remains an essential strategic partner to the U.S., but that in matters of energy security, "we cannot be more European than the Europeans." He also emphasized that the Central and Eastern European (CEE) EU members - with the most at stake in the formulation of a coherent EU policy on energy security - need to be unified and lead the EU in the right direction on this issue. Regarding Russia, raised as a concern by numerous contacts, Morningstar was clear that our desire to engage the Russians will not be at the expense of our principles. End summary.

BAJNAI: CONCERNED ABOUT EU WAVERING ON NABUCCO, GROWING
RUSSIAN INFLUENCE IN BALKANS

[1](#)2. (C) Ambassador Morningstar held a wide-ranging discussion on Hungarian and Central European energy security with Prime Minister Bajnai. Morningstar stressed the importance of Hungarian leadership in forging CEE cooperation on energy security. Bajnai emphasized that Nabucco remains Hungary's top priority and expressed frustration with the lack of consistent EU support for the project. Listing the challenges the project faces, such as uncertainties about gas supplies, transit across Turkey, and project financing, he stressed that strong EU backing is needed to counter a very efficient, well coordinated Russian communication strategy that sows doubt among current and potential Nabucco partners and convinces them to diversify by signing up for South

Stream. According to Bajnai, Energy Commissioner Piebalgs was not active enough on the issue and the EU has been remiss in failing to fill the vacancy left by former EU Nabucco Coordinator Van Aartsen. He plans to write a letter to Commissioner Barroso to advocate for the appointment of an EU Special Representative for Nabucco and for EU support for establishing a Nabucco International Board, which he hopes to announce at the January conference of V-4 prime ministers. In response to Bajnai's request for U.S. help in pushing for a permanent EU structure to support Nabucco, Morningstar promised to raise the issue in his upcoming meetings in Brussels. Morningstar added that the EU could also play a helpful role in resolving gas supply and transit questions in Azerbaijan, Turkey, and Iraq.

13. (C) Turning to Russian Surgutneftegaz' (SNG) attempt in March to mount a hostile takeover of MOL (ref A and B), Bajnai said the GOH had assumed the burden of defending MOL. He indicated that he intends to discuss the matter with Putin, but he has not yet had the opportunity to do so. In addition to the suspicious SNG transaction, he said he would seek clarification from Moscow on the sale of shadowy Hungarian gas trader Emfesz to previously unknown Swiss-registered Rosgas, which in Bajnai's view is linked to Gazprom.

14. (C) Bajnai expressed deep concern about recent Russian efforts to gain influence in Croatia's energy sector (ref C), which he characterized as "the cornerstone of Hungarian strategy." He confirmed that he plans to discuss the matter

BUDAPEST 00000843 002 OF 006

and its potential impact on Croatian EU accession with the Croatian PM Kosor. He will also invite Croatia to a January meeting of Visegrad-4 (V-4) Prime Ministers, which will include a discussion on energy security.

15. (C) Bajnai is hopeful that a deal on Ukrainian gas payments to Gazprom might avert a repeat of last winter's gas cutoff, but he agreed with Morningstar that similar problems are likely to occur in the future unless Ukraine undertakes fundamental reforms in its energy sector. According to Bajnai, the only thing that has changed in recent years is that Ukraine's pipeline network has deteriorated, providing some justification for new pipelines to circumvent it. He acknowledged, however, that cutting Ukraine out of Europe's energy equation would further diminish the prospects for Ukrainian political and economic reform.

16. (C) Bajnai believes the Western Balkans, like Ukraine, need the carrot of European/Atlantic integration to keep on the right track. Morningstar conveyed the Macedonian DPM Peshevski's concerns about gas supplies (paragraph 22 below) and recommended that the EU engage in a discussion of how Nabucco and ITGI might address Balkan gas needs as well as the appropriate sequencing of the two pipelines. Bajnai pointed out that Hungary is already cooperating with its Balkan neighbors by building a gas connection with Croatia and allocating some of its gas storage capacity to supply Serbia in the event of a gas supply disruption.

ORBAN: LIKELY TO FOCUS ON INDEPENDENT, PRAGMATIC RUSSIAN POLICY OVER CEE LEADERSHIP

17. (C) Fidesz President and former (and probable future) Prime Minister Viktor Orban, joined by former (and probable future) Economy Minister Gyorgy Matolcsy and Parliamentary Foreign Affairs Committee Chairman Zsolt Nemeth, met with Ambassador Morningstar to discuss how a Fidesz government might address energy security and Russian relations after the general election next spring. Orban agreed with Morningstar on the need for greater CEE unity in EU policymaking but said an EU policy on energy security would continue to be complicated by a lack of trust among EU partners arising from the numerous bilateral deals many have already concluded with Russia.

¶18. (C) In Orban's view, the Central Europeans need to become more action-oriented in their approach, which he believes has been dominated until now by "tortured intellectuals" theorizing about a "grand architecture" for cooperation. Orban said he would start with smaller, more achievable projects and build from there. He would also let the Poles lead because "they deserve it and they think they deserve it," and also because they would be more likely to bring the Slovaks on board. This would also allow Hungary to focus on its Balkan neighbors to the south. According to Orban, one such area for cooperation would be the establishment of an energy security fund to support regional energy security projects and to protect against the hostile takeover of strategic national companies such as MOL.

¶19. (C) Orban and Nemeth each emphasized Nabucco's importance to Hungary's energy diversification strategy, but neither indicated any intention to revise official Hungarian policy on South Stream assuming Fidesz wins the general elections next year. According to Orban, Nabucco is the top priority because it represents source diversification, but Hungary cannot risk being left out of South Stream, even if it ultimately comes at the expense of Nabucco. In response to Nemeth's suggestion that U.S. capital might help move Nabucco forward, Morningstar clarified that there will be no U.S. subsidies for the Southern Corridor, although if U.S.

BUDAPEST 00000843 003 OF 006

companies do participate in any way, U.S. government resources like OPIC or ExIm Bank could be explored.

¶10. (C) Matolcsy understood that the U.S. could not subsidize a European pipeline project, but said that Hungary could greatly benefit from U.S. technologies in renewable energy and energy efficiency. Morningstar agreed and said such cooperation would be a key element of the EU-US Energy Council, but that it could also happen on a bilateral basis.

¶11. (C) Further elaborating his approach to Russia, Orban said he would pursue a clearcut, transparent intergovernmental agreement with Moscow on bilateral trade and investments. According to Orban, Hungary's trade deficit with Russia--mainly due to energy imports--is too large to correct by market means and instead requires government intervention. He stated that Fidesz, anticipating that it will form a government in about five months, has already begun to engage Moscow on commercial matters and stipulated that Hungarian national champions MOL (oil and gas), OTP (banking), and Richter (pharmaceuticals) are off-limits to hostile takeover by Russian firms. (Note: Orban traveled to St. Petersburg over the weekend of November 21 to attend the congress of the United Russia Party and meet with the party's chairman, Prime Minister Putin. End note.)

¶12. (C) Responding to Morningstar's question about how the U.S. can help the CEE region on energy security, Orban requested U.S. assistance in fostering greater political cooperation among the CEE countries. Remarking that he was disappointed about the change in U.S. missile defense policy in Central Europe, Orban suggested that U.S. participation in the proposed energy security fund would also be a good way to demonstrate backing for the region's energy security. (Comment: Apart from the request for a U.S. financial contribution, Orban did not elaborate on funding sources or specific projects that such a fund might support. Neither was it clear how this concept would satisfy his stated preference to base cooperation on small, concrete, achievable projects. End comment.)

¶13. (C) Nemeth added that U.S. diplomacy was a key factor in delivering a Turkish signature to the Nabucco IGA and requested our ongoing assistance in helping the Turks and Azeris agree on a gas transit regime. He also asked for U.S. help in countering recent Russian moves to gain influence in Croatia's energy sector, which he says puts the proposed Krk

liquefied natural gas facility at risk.

MOL: GOVERNMENT, EU SUPPORT NEEDED TO COUNTER RUSSIAN PRESSURE, KICKSTART NABUCCO FINANCING

¶14. (C) Ambassador Morningstar met with Hungarian Oil Company (MOL) CEO Zsolt Hernadi, Chief Strategist Laszlo Varro, and CEO Advisor Reka Szemerkenyi to discuss MOL's efforts to resist a Russian takeover following the purchase by Surgutneftegaz (SNG) last March of a 21 percent stake in the company. Hernadi revealed that Russian Deputy Prime Minister/Rosneft CEO Igor Sechin had told him personally that MOL is not just fighting against SNG, but against the Russian state, which can employ tools that companies may lack. Sechin then added that if MOL was uncomfortable with SNG as an investor, then perhaps a more suitable Russian company could take its place. Hernadi clearly views SNG as a hostile suitor, despite his recent public comments ascribing more benign motives behind the SNG stake in MOL, and he appreciates the political consensus for a robust government-backed defense of the company. He noted that Bajnai and Orban allowed the "blame" for the blocked takeover attempt to be shifted to the Hungarian state, which retains veto rights over changes to the composition of MOL's Board of

BUDAPEST 00000843 004 OF 006

Directors and corporate structure. Moreover, the Hungarian Energy Office continues to refuse registration of the SNG ownership in MOL due to the lack of transparent information on SNG's own ownership.

¶15. (C) Hernadi described recent Russian efforts to gain influence in Croatia's energy sector partly as an effort to break the stalemate on the MOL acquisition. He refuted recent reports in the international press that MOL might swap its 47 percent stake in Croatian oil and gas company INA for SNG's stake in MOL. Croatia remains essential to MOL's corporate strategy as the Adria pipeline provides MOL with its sole source of non-Russian oil imports; the proposed Krk LNG terminal and Hungary-Croatia gas interconnector, which is currently under construction, would allow non-Russian gas imports; and INA's strong upstream oil and gas presence complement MOL's downstream strengths.

¶16. (C) Hernadi is very concerned that Russia is seeking a strategic foothold by offering the new Croatian government "carrots" such as South Stream, new oil and gas contracts at reduced prices, and investments in refinery upgrades. He believes Russia's likely targets include the government's 45 percent stake in INA as well as the 75 percent government-owned oil pipeline operator Janaf, which controls the Adria pipeline and Omisalj oil terminal on Krk island, the site of the proposed LNG terminal. According to Hernadi, the GOH, one of the primary sponsors of Croatian EU accession, is already engaging Zagreb to warn that excessive Russian control of the energy sector could weaken accession prospects. To provide a counterweight to the frequent meetings ongoing between Zagreb and Moscow, the GOH, as current president of the V-4, is planning to involve Croatia in upcoming minister-level and PM-level meetings in December and January, respectively. Hernadi remains concerned, however, that the EU continues to view the Croatian developments as a "business issue" rather than as a "strategic issue."

¶17. (C) Turning the conversation to EU support for Nabucco, Hernadi, as a former banker, said Nabucco would never be able to obtain necessary financing without a more significant EU financial commitment. Varro suggested past EU financing for projects such as Airbus and Galileo as a possible model, whereby the EU could provide loans on preferential terms that would be paid back by royalties once the project begins producing income. The EU, however, still does not treat the project as one with strategic/security implications. Ambassador Morningstar reiterated his point that it is up to the Central Europeans, who have the most at stake, to present

a united front in the next EU budget negotiation and, if necessary, to block passage of an EU budget until their needs are addressed. Moreover, the Central Europeans should play a similar game of hardball with Croatia regarding its EU accession aspirations.

BAYER: RUSSIA USING SOUTH STREAM TO DIVIDE AND CONQUER

¶18. (C) Hungarian Ambassador-at-Large for Energy Security Mihaly Bayer described recent Russian efforts to conclude South Stream agreements with additional countries, such as Turkey, Croatia, Slovenia, and Austria, as an effort to introduce ambiguity into the pipeline's likely route to extract further concessions from potential participants. According to Bayer, once the agreements are signed, host countries will be selected based on who has offered the most.

Bayer is warning his counterparts in Serbia and Croatia about placing too many eggs in the Russian basket. Allowing too many strategic assets to fall into Russian hands could affect EU accession prospects, while the promised South Stream might never be built, or if it is, it could still pass

BUDAPEST 00000843 005 OF 006

them by.

¶19. (C) Responding to Ambassador Morningstar's question about Orban's prospects for leading a CEE coalition within the EU, Bayer said Orban will need to navigate successfully thorny Hungarian minority issues that have complicated past relations in Hungary's neighborhood and closely coordinate policies with Poland, which is probably a more natural leader owing to its size and its proactive foreign policy. Bayer believes Orban will avoid clashes with Russia, preferring instead a balanced, pragmatic approach based on mutual interests and respect.

EU NEEDED TO SPUR SOUTHERN CORRIDOR, ENSURE NON-EU INTERESTS ALSO CONSIDERED

¶20. (SBU) During a roundtable lunch with Bayer, Koka, Bulgarian Energy Envoy Poptchev, Macedonian Deputy Prime Minister Peshevski, and Slovak Ambassador Weiss, Ambassador Morningstar raised for discussion questions of compatibility and sequencing between Nabucco and the Italy-Turkey-Greece Interconnector (ITGI). Bayer argued that ITGI is a competitor to Nabucco because it establishes the precedent for Turkish offtake of 15 percent of the Azeri gas flowing into the pipeline, which the Nabucco project is trying to avoid. Furthermore, the completion of ITGI would allow European countries without a stake in Nabucco to "check the Southern Corridor box" without really accomplishing its full purpose, he said. Bayer noted a preference toward ITGI among people in Brussels who are working on the Southern Corridor.

¶21. (SBU) Poptchev added that any hint of competition between the two projects should be avoided and that efforts should be made to convince Italy to allow Nabucco to be built first. Ambassador Morningstar suggested that talks between the Nabucco and ITGI consortia on sequencing might be helpful, but highlighted a potential political barrier to cooperation given that Italian companies ENI and Edison are involved in South Stream and ITGI, respectively. Bayer added that the U.S. could be helpful in encouraging the Nabucco and ITGI consortia, the European Commission, and the Italians to work out the projects' sequencing, particularly given Commissioner Barroso's strong support for Nabucco.

¶22. (SBU) Macedonian DPM Peshevski made a case for connecting Macedonia to the ITGI pipeline to cover its own gas needs--Macedonia's existing import pipeline, controlled by Gazprom, currently operates at 6 percent of capacity--and to provide a link to supply Kosovo. Bayer echoed the importance of including the Western Balkans in the Southern Corridor calculus. Ambassador Morningstar noted that this discussion demonstrated that not all countries' interests were being represented at the EU level and underscored the need for

closer coordination among the CEE countries on energy security policy within the EU.

¶23. (SBU) In a separate meeting, Parliamentary Nabucco Committee Chairman Janos Koka told Ambassador Morningstar of his efforts to establish a Nabucco International Board (NIB) to maintain political momentum and coordinate the fragmented European approaches toward the project. Although the Hungarians managed to insert a reference to the NIB into the Intergovernmental Agreement, the body has yet to take shape. Ambassador Morningstar suggested that a more meaningful gesture of European seriousness toward Nabucco would be to have six or eight EU prime ministers travel together to Turkey and the Caspian region. Koka provided a short read-out of a recent trip to Egypt in which he learned of an upcoming tender for offshore gas exploration. According to Koka, the Egyptians would like to provide 3-6 billion cubic meters per year for Nabucco through the Arab pipeline.

BUDAPEST 00000843 006 OF 006

TOPOLANEK: U.S. PRESENCE NEEDED TO COUNTER RUSSIA IN CENTRAL EUROPE

¶24. (C) Former Czech Prime Minister Mirek Topolanek expressed serious concern over what he termed "a strengthening of post-Yalta demarcation lines" in Europe. He highlighted several examples of resurgent Russian influence in Central and Eastern Europe, including acquisitions of strategic economic and energy assets, an increased intelligence presence, efforts to influence domestic politics in CEE and neighboring countries, and what he termed an "emancipation" of Russia on the international political scene to pursue its geopolitical objectives unchecked. To counter this trend and to compensate for a lack of EU unity toward Russia, Topolanek requested that the U.S. employ pressure as part of its strategy to engage Russia and pressed for a strong U.S. physical presence in Central Europe. Topolanek said it would be ideal to see Westinghouse participate in the new nuclear projects planned in the region and insisted that the choice of Russian fuel for the Temelin reactors was based purely on the poor quality of the Westinghouse fuel. Responding to Ambassador Morningstar's point that the CEE countries could be more effective in having their interests represented in the EU if they coordinated their policies better, Topolanek said they would first need to overcome their "inferiority complex" in relation to larger, wealthier Western partners. He added that probable future Hungarian Prime Minister Viktor Orban might be able to provide needed CEE leadership as long as his tendencies toward nationalism did not interfere.

CONTINUED U.S. ENGAGEMENT NEEDED

¶25. (C) Comment: Ambassador Morningstar's interlocutors agreed with his assessment that closer cooperation among the CEE countries and a united front within the EU is the only way to ensure the strategic issue of regional energy security garners the attention it deserves in Brussels. Many, however, were less certain about who should lead this effort.

Few, including Orban himself, seemed to expect an Orban government to rally a CEE coalition. Despite conference chair Janos Csak's remark in his opening statement that the U.S. should not have to function as the region's "kindergarten teacher," all interlocutors indicated that ongoing U.S. engagement would be essential to helping the CEE countries see that their energy security needs are met within the EU. To that end, all welcomed Ambassador Morningstar's possible participation in next January's meeting of V-4 prime ministers. A possible visit by MOL CEO Hernadi to Washington in February 2010 could be an additional opportunity for the U.S. to engage a key private sector player in Central Europe's energy security picture. End comment.

¶26. (U) Ambassador Morningstar has cleared on this cable.
LEVINE